

## ANALYSIS OF AMENDED BILL

### Franchise Tax Board

Author: Ashburn Analyst: Angela Raygoza Bill Number: SBX2 15  
Related Bills: See Legislative History Telephone: 845-7814 Amended Date: February 15, 2009  
Attorney: Patrick Kusiak Sponsor: \_\_\_\_\_

**SUBJECT:** Qualified Principal Residence Purchase Credit

### SUMMARY

This bill provides a credit under the Personal Income Tax Law (PITL), as specified, to an individual who is a purchaser of a qualified principal residence.

### SUMMARY OF AMENDMENTS

The February 15, 2009, amendments would provide a tax credit for the lesser of 5% of the purchase price of a qualified residence, or \$10,000, as specified.

The bill as introduced on February 11, 2009, expressed the intent of the Legislature to make changes related to the 2009 budget.

This analysis addresses the bill as amended February 15, 2009. This is the department's first analysis of this bill.

### PURPOSE OF THE BILL

According to author's office, the purpose of the bill is to encourage sales of previously unoccupied single-family residences.

### EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill is effective immediately, and specifically operative for purchases of qualified principal residences made on or after March 1, 2009, and before March 1, 2010.

### POSITION

Pending.

#### Board Position:

_____ S	_____ NA	_____ NP
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#### Department Director

#### Date

Selvi Stanislaus

02/27/09

## **ANALYSIS**

### **Federal Law**

#### First-Time Homebuyer's Credit

##### Housing and Economic Recovery Act of 2008 (Public Law 110-289)

A “first-time homebuyers” credit was enacted by the Housing and Economic Recovery Act of 2008. The Act added a new refundable tax credit for “first-time homebuyers.” The amount of the credit is the lesser of \$7,500 or 10% of the home’s purchase price. The credit is phased out for taxpayers with adjusted gross income<sup>1</sup> (AGI) between \$75,000 and \$95,000 (\$150,000 and \$170,000 for joint filers). The credit applies to principal residences purchased after April 8, 2008, and before July 1, 2009.

The credit is recaptured under the terms of Internal Revenue Code (IRC) section 36(f) over 15 years with no interest charge, beginning with the second tax year after the tax year in which the home is purchased. If the home is sold before the 15-year period ends, the remaining credit must be recaptured in the year of sale.

##### American Recovery and Reinvestment Act of 2009

The “first-time homebuyers” credit was modified by the American Recovery and Reinvestment Act of 2009. In general, for homes purchased before December 1, 2009, the maximum credit is increased to \$8,000 (\$4,000 for a married individual filing separately), the credit is no longer recaptured unless the taxpayer sells the home within 36 months, and the credit can apply to homes that are financed by exempt mortgage revenue bonds or located in the District of Columbia.

### **State Law**

Existing state law does not provide a comparable “first-time homebuyer’s” credit.

Existing state and federal laws provide various tax credits designed to provide tax relief for taxpayers who incur certain expenses (e.g., child adoption) or to influence behavior, including business practices and decisions (e.g., research credits or economic development area hiring credits). These credits generally are designed to provide incentives for taxpayers to perform various actions or activities that they may not otherwise undertake.

Current state law limits the amount of allowable tax credits for each taxable year beginning on or after January 1, 2008, and before January 1, 2010, to an “applicable amount.” “Applicable amount” is equal to 50% of the tax before the application of any credits. Any disallowed credit remains a credit carryover to subsequent years and the credit carryover period is increased by the number of taxable years the credit amount was disallowed. Taxpayers with business income subject to tax of less than \$500,000 are excluded from this law.

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<sup>1</sup> Adjusted Gross Income as defined by IRC section 62 means gross income minus deductions.

## THIS BILL

This bill would provide a credit under the PITL to an individual who is a purchaser of a qualified principal residence. The amount of the credit would be equal to the lesser of 5% of the purchase price of the qualified principal residence or \$10,000.

The bill would require that the credit be claimed in equal amounts over three taxable years, beginning with the taxable year in which the purchase of the residence is made.

The credit would be allowed for one purchase of a qualified principal residence by an individual and would apply to purchases made on or after March 1, 2009, and before March 1, 2010.

This bill defines “qualified principal residence” as a single-family residence that is all of the following:

- Either detached or attached,
- Never been occupied,
- Purchased to be the principal residence of the purchaser for a minimum of two years, and
- Eligible for the homeowner’s exemption.<sup>2</sup>

Within one week of the sale of the qualified principal residence, the seller would be required to provide to the purchaser and to FTB certification that the residence has never been previously occupied.

The credit would be denied if the taxpayer fails to occupy the qualified principal residence as his or her principal residence for at least two years immediately following the purchase. In such case, the taxpayer is liable for any credit allowed in previous years.

In the case of two married taxpayers filing separately, the credit would be equally divided between the taxpayers. If two or more taxpayers who are not married purchase a qualified principal residence, the credit would be allocated among the taxpayers in the same manner as each taxpayer’s percentage of ownership, but the total allocated credit may not exceed \$10,000.

The total credit that would be allowable is limited to \$100 million. Upon receipt of certification from the seller, FTB would allocate the credit based on a first-come, first-serve basis. The credit must be claimed on a timely filed original return. The determination by FTB with respect to the date a certification is received, and whether a return has been timely filed, may not be reviewed in any administrative or judicial proceeding.

Any disallowance of a credit claimed on the basis of exceeding the \$100 million limitation would be treated as a mathematical error and any tax resulting from such disallowance may be assessed in the same manner as applicable to mathematical errors. Any disallowance may not be protested or appealed.

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<sup>2</sup> R&TC section 218.

The credit would not be a business credit for purposes of the 50% business-credit limitations.<sup>3</sup>

FTB may prescribe rules, guidelines, or procedures necessary or appropriate to administer the credit. Those rules, guidelines, and procedures are exempt from provisions of the Administrative Procedures Act regarding regulations.

The provisions of this bill would remain in effect until December 1, 2013, and as of that date would be repealed.

## LEGISLATIVE HISTORY

SB 49 (Dutton, 2009/2010) would provide a credit similar to the one provided by this bill. That bill is currently at the Senate Revenue and Taxation Committee.

## OTHER STATES' INFORMATION

*Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York* laws do not provide a credit comparable to the credit allowed by this bill. The laws of these states were reviewed because their tax laws are similar to California's income tax laws.

## FISCAL IMPACT

Implementing this bill would require FTB to create a new process to allocate credits when the seller submits a certification that the property sold was unoccupied. FTB would be required to create new forms, develop a secure transmission process for the receipt of the certifications, and change systems to account for the new credit. FTB estimates the costs to the department to implement this bill would be approximately \$267,000 in first year (2.6 PY) and approximately \$15,000 of ongoing costs (.3PY).

## ECONOMIC IMPACT

### Revenue Estimate

Based on the data and assumptions discussed below, this proposal would result in the following revenue losses:

Estimated Revenue Impact Qualified Principal Residence Purchase Credit Effective for Homes Purchased between March 1, 2009 and March 2, 2010 Assumed Enactment Date Before 2/28/09 (\$ in Millions)			
2008/09	2009/10	2010/11	2011/12
-\$2	-\$11	-\$11	-\$9

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<sup>3</sup> R&TC section 17039.2.

This analysis does not consider the possible changes in employment, personal income, or gross state product that could result from this bill.

### Revenue Discussion

The revenue impact of this bill would depend on the number of taxpayers that purchase a new or previously unoccupied single-family home. The home must serve as a primary residence and be purchased on or after March 1, 2009, and before March 1, 2010.

Based on historical data from the California Builder's Association for 2008 and using the Department of Finance's growth projections for new home sales, it is estimated that approximately 27,000 new homes will be sold during 2009 in California. To exclude investment purchases, because qualified purchases must serve as a taxpayer's primary residence, projected new home sales for 2009 would be reduced by 5% to 25,650  $[27,000 \times (1 - 5\%)]$ . Because qualified purchases are limited to those made after March 1, 2009, total sales for 2009 would be reduced by 17% (2 months / 12 months) to 21,300  $[25,650 \times (1 - 17\%)]$ . Using the same methodology and reducing the figures to reflect purchases made by March 1, 2010, qualified purchases for taxable year 2010 are approximately, 6,000 (38,631 new home sales projection for 2010 x 95% to exclude investments x 17% to include only January and February purchases).

To determine the value of credits generated and used, taxpayers with no tax liability were excluded. Tax data for individuals who reported the mortgage interest deduction for tax year 2005 was analyzed finding that approximately 75% of these filers had a tax liability. Applying this statistic to the estimate of qualified purchases for taxable year 2009, it is assumed that 15,975  $(21,300 \times 75\%)$  purchasers would have a tax liability and approximately 5,000  $(21,300 \times 24\%)$  would not. Applying the credit limitation of \$10,000, generated credits would total approximately, \$160 million  $(15,975 \times \$10,000)$ .

Because this bill would limit the amount of credit allowed to \$100 million, the total amount of credit allocated would only be \$100 million. It is assumed that one-third of the homebuyers who do not have a tax liability will receive certification for the credit. Thus, of the \$100 million allocation, approximately \$16 million would be allocated to homebuyers who do not have a tax liability  $(5,000 \text{ homebuyers} \times 33\% \times \$10,000 = \$16 \text{ million})$ . However, because it is estimated that the \$100 million cap would be depleted prior to the end of 2009, it is estimated that only \$11 million of the \$100 million cap would be allocated to homebuyers who do not have a tax liability.

The remaining \$89 million would be claimed — one-third each year — by taxpayers on their 2009, 2010, and 2011 tax returns. For the 2009 taxable year, it is estimated that there would be approximately \$30 million in credits claimed  $(\$89 \text{ million} \times 33\%)$  and approximately \$13 million in credits used to offset tax. It is estimated that, on average, taxpayers would be able to use approximately 38% of the credit claimed each year. For the 2009 taxable year, it is estimate that there would be approximately \$11 million in credits used to offset PIT taxes  $(\$30 \text{ million} \times 38\% \approx \$11 \text{ million})$ .

Revenue losses for the next two years would be comparable, slightly over \$11 million per year. The figures in the chart have been adjusted to reflect the cash flow impact on a fiscal-year basis. The revenue loss for fiscal year 2009/10 includes credits used to reduce tax year 2009 liabilities and reduced estimated payments for tax year 2010 liabilities.

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